

# Pest analysis of russian retail market

Business



PEST Analysis The PEST analysis is used in this report to evaluate the political, economic, social and technological aspects of the macroeconomic environment in the targeted market, Russia. This study helps to frame the basis for the decision-making about a possible market entry. Thus, it is of vital importance to scrutinize the macroeconomic environment as part of the market research. Political and Legal Aspects According to the Russian 1993 Constitution, Russia is a democratic federative state with a republican form of government grounded in the rule of law (pwc, 2012).

After the fall of the Soviet Union in 1991, Russia has gradually opened up and after a seven-year transitional period with numerous market reforms, political stability was achieved under Prime Minister Putin and President Medvedev. Moreover, since 1999 when Putin became president for the first time, Russia's political system has shown continuity in its policies. The Russian judicial system is based on statutory law, but has been ineffective and weak since the fall of the Soviet Union. However, the introduction of many reforms is expected to eventually bring about improvements.

Russia has also entered various legal assistance programs with countries across the world, as unfair competition practices are hindering FDI inflows into the country (Datamonitor, 2011; pwc, 2012). However, corruption and crime are still major challenges for doing business in Russia. Russia has been ranked 143rd in Transparency International's corruption perception index of 2011 concerning perceived public sector corruption. In addition, the high degree of bureaucracy within the country makes doing business slow and complicated.

The business environment is further negatively affected by the high number of corrupt state officials (Datamonitor, 2011). Terrorist activity is one of the major concerns in Russia as bomb explosions and suicide attacks (such as those in the Moscow-St. Petersburg express train in 2009 or in the Moscow metro in 2010) have killed dozens of people over the last years (Datamonitor, 2011). Russia is member in many different international, regional, economic and financial agreements such as G8, G20, and International Monetary Fund just to name a few of them. (pwc, 2012) The country further integrated within the world economy by entering the World Trade Organization (WTO) in 2012 (Datamonitor, 2011). Economic Aspects Russia of 2011 is characterized by a per capita GDP (PPP) of \$16,750, GDP and FDI growth of 4.3% and 33% respectively. Furthermore, the ease of doing business in the country improved by 4 ranks between 2011 and 2012 and hence Russia is ranked 112th in 2012 (Datamonitor, 2011; pwc, 2012). Historically successful economic reforms during the 1990s led to liberalization of the Russian economy and to high growth rates.

Yet, the global economic downturn beginning in 2008 led to a negative growth of 7.7% in 2009. However, the country's economy managed to quickly recover, achieving a 3.9% GDP growth in 2010, mainly due to the high oil prices (Datamonitor, 2011). Improved competitiveness and higher oil prices facilitated a turnaround in the current account, from a deficit in 1998 to a surplus of 12% of GDP in 1999. Since 2000, Russia has maintained a current account surplus, which dropped from around \$102bn in 2008 to around \$47bn in 2009 (Datamonitor, 2011; pwc, 2012).

Current challenges in Russia's economic landscape include a high budget deficit and a banking system being under continuous stress. Moreover, the unemployment rate of 6.6% is another negative side of Russia's economic landscape (Datamonitor, 2011). Social Aspects The main ethnic group within Russia is Russians with 79.8%, while other ethnic groups include Tatar 3.8%, Ukrainian 2%, Bashkir 1.2%, Chuvash 1.1%, other or unspecified ones with 12.1% (2002 census) (CIA The World Factbook, 2012).

Concerning religion, estimates from 2006 suggest that 15-20% of the population are Russian Orthodox, 10-15% are Muslim, and 2% - other Christian, yet large parts of the population are non-believers, a likely legacy from the Soviet era (CIA The World Factbook, 2012). The United Nations Development Program (UNDP) ranks Russia 66th with regards to overall human development, making Russia part of the high human development quartile. However, one major challenge within Russia is the huge gender gap concerning life expectancy.

Average life expectancy is 66.2 years, yet it is only 59.8 years for men, while boosting 73.1 for women (United Nations Development Program (UNDP), 2011; Datamonitor, 2011). Russia is estimated to be one of the fastest-growing countries concerning proportion of population to be considered middle class. (Financial Times - Chart of the week: tracking the rising EM middle classes, 2012). The related increase in disposable income can be illustrated by the tripling in middle class spending between 2000 and 2010.

However, the widening income inequality may pose a challenge for long-term success (Datamonitor, 2011). In general, Russia's current strengths

concerning social development are the high level of social governmental spending and the well-educated population. However, the country still struggles with a high mortality rate and a widening income inequality gap (Datamonitor, 2011). Technological Aspects Russia has signed the TRIPS (Trade-related Aspects of Intellectual Property) agreement, but nevertheless faces Intellectual Property Rights issues regularly.

Moreover, the country still lacks adequate telecommunications infrastructure (Datamonitor, 2011). PEST Implications for the Retail Industry Russia's political and legal framework suggests that foreign retail operations in Russia, although not restricted, may be inefficient because of bureaucracy and corruption. In addition, the usage of the ruble exposes foreign investors to exchange rate risks. The economic characteristics of the Russian market, however, paint a much more attractive picture of the industry, which represents 15. % of the country's GDP. The Russian retail and wholesale sector has attracted 17. 1% of the country's FDI in 2011. The country also has the lowest retailer penetration rates in Europe (pwc, 2012), suggesting it is a market in its growth stage with significant opportunity for new entrants. Yet, a recent study conducted by the management consulting group, AT Kearney, shows that Russia has fallen behind BRIC and other emerging market nations in terms of the countries' attractiveness for investments in the retail sector.

In fact, it ranks 26th out of 30 emerging market nations with regard to the attractiveness of the retail sector. As some experts argue such a ranking may reflect the strong foothold of local retailers, with such rivalry making the Russian retailer market a developed rather than an emerging one (Financial

Times - Russia retail: losing appeal, 2012) The pending commercialization of the cloud-dispersal aircraft technology may also have a positive trickle-down effect on the retail industry.

The technology may solve the problem of drought-prone areas, representing 6% of arable land within Russia, possibly improving domestic food production, and supplier reliability (Data Monitor, 2011; CIA The World Factbook, 2012). Overall, the country environment suggests that despite some institutional voids, the economic environment is conducive to a booming retailer segment with a growth that can be exploited by foreign retailers. The decrease in FDI attractiveness, however, points to the likely presence of established competitors that may prevent such an entry, which will be analyzed in greater detail in the industry analysis.